No. 10289

In the United States Circuit Court of Appeals for the Ninth Circuit

Lombard Trustees, Ltd., a Trust, and Charles S. Lombard, Bertha M. Lombard and Norman M. Lombard, Trustees thereof, petitioner

v.

Commissioner of Internal Revenue, respondent

ON PETITION FOR REVIEW OF THE DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

SEWALL KEY,
HELEN R. CARLOSS,
IRVING I. AXELRAD,
Special Assistants to the Attorney General.

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CITATIONS

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OPINION BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 53–73) is unreported.

JURISDICTION

This petition for review (R. 75–77) involves federal income and excess profits taxes for the taxable year 1937. On June 15, 1940, the Commissioner of Internal Revenue mailed to the taxpayer notice of a deficiency in income tax in the amount of $5,001.09 and excess profits tax in the amount of $2,015.10. (R. 1–2.) Within ninety days thereafter, the taxpayer filed a peti-

tion with the Board of Tax Appeals for a redetermination of that deficiency under the provisions of Section 272 of the Internal Revenue Code. The final order and decision of the Board of Tax Appeals sustaining the deficiency in income tax and excess profits tax in the respective amounts of $5,818.66 and $258.14 was entered on June 19, 1942. (R. 74.) The case is brought to this Court by a petition for review filed September 8, 1942 (R. 75–77), pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

QUESTION PRESENTED

Whether the taxpayer, Lombard Trustees, Ltd., was an association, and therefore taxable as a corporation during the entire taxable year 1937, within the meaning of Section 1001 (a) (2) of the Revenue Act of 1936, as determined by the Commissioner and held by the Board of Tax Appeals, or a pure trust and taxable as such, as claimed by the taxpayer.

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved will be found in the Appendix, *infra*, pp. 36–42.

STATEMENT

The findings of fact of the Board of Tax Appeals (R. 54–65) were based on the stipulations of facts (R. 54.) These facts, as found by the Board or in the stipulations, may be summarized as follows:

Charles S. Lombard, hereinafter called Dr. Lombard, and Bertha M. Lombard were married in 1907 and reside in Redlands, California. Three children, Emily,

Winthrop and Ruth, were born of this marriage. Bertha Lombard also had two children, Ralph and Dorothy Pray, born of a former marriage, and Dr. Lombard had four other children born of a former marriage. They are Lillis Stowe, George Lombard, Charles S. Lombard, Jr., and Norman Lombard. Dr. Lombard was 83 years old in 1935 and Bertha Lombard was 63. The ages of the above children range from 52 to 22 years. (R. 54.)

In 1935 Dr. Lombard learned of a copyrighted printed plan called the "Hulbert Plan Trust," a copy of which he purchased from a representative of the publisher in San Bernardino. On November 3, 1935, Dr. Lombard and Bertha Lombard, as grantors, and Winthrop, Emily and Norman Lombard, as trustees, executed the "Hulbert Plan Trust." From that date and during the entire taxable year 1937 the agreement was operative and in full force and effect. On November 3, 1935, the day that the agreement was executed, two of the trustees, Emily and Winthrop Lombard, resigned and Dr. and Bertha Lombard succeeded them and with Norman Lombard have acted as trustees since. On November 3, 1935, also, Dr. Lombard conveyed to the trustees one parcel of business property and at other times during 1935 he conveyed six other pieces of business property, including an orange grove, and on December 31 he transferred securities. The real and personal property owned by Dr. Lombard at the beginning of 1935 was valued at $300,000. The dates, value, and description of the gifts made to the trust in 1935 are shown, *infra*, as reported by Dr. Lombard on his gift tax return for 1935. (R. 55, 61.)

The conveyance and agreement of November 3, 1935, was recorded on November 14, 1935, in the office of the recorder at San Bernardino County. All of the parties to the agreement were residents of California, and all property conveyed to the trustees pursuant to the agreement was located in California. (R. 55.)

The "Hulbert Plan" was a series of legal instruments rather than a trust indenture. The first instrument, entitled "Conveyance and Contract," was executed by Dr. and Bertha Lombard. By this agreement they, as "grantors," appointed three trustees who were to use in their collective capacity the trade name, Lombard Trustees, Ltd. The "grantors" conveyed to the "trustees" for $100 and other valuable consideration, property described in a "deed" which was made part of the instrument. The "grantors" sold, assigned and conveyed the property to the "trustees" as joint tenants and as "the exclusive owners" with power to sell, mortgage, and encumber the property in their own discretion, "without hindrance from, submission to, or approval of 'beneficiaries.'" The document expressly stated that the "trustees" should be unrestricted in their ownership, control, administration and disposition of the "estate." (R. 55–56.)

The second instrument was executed by the "grantors" and the "trustees," and comprises an "Acceptance" by the "trustees" and a "Contract containing Articles of Administration" to which the "trustees" agreed. The "trustee" accepted their appointment and the property conveyed to them and they agreed to "conserve," "handle and barter," "manage and administer" the property and its accretions. (R. 56.)

The "trustees" agreed with each other in "Articles of Administration" which provided that the "trustees" should "be construed to be the absolute and exclusive owners, in joint tenancy and continuity, of the legal and equitable title to all property, real and personal in the Estate." The document authorized the "trustees" to act in their trade name through authorized officers, to hold regular and special meetings and to adopt and use a seal. (R. 56–57.)

The Articles set forth the general power of the "trustees" as follows (R. 57):

> Art. 3. Powers: Being Natural Persons these Trustees, their associate and/or successor Trustees, shall organize themselves into a Board, and may do collectively, in their discretion, any lawful things which citizens may lawfully do in any or all States unless herein limited. (It should be remembered: "Corporations possess only such powers as are granted to them by law, while individuals possess all powers except those prohibited by law.") They may own real estate or personal property in any State without limit, may buy, sell, improve, exchange, assign, convey and deliver, may grant trust deeds and may mortgage or otherwise encumber for obligations; may own stock in or entire charters or corporations, and may engage the Estate funds and properties in any industry or investment in their discretion, *hoping thereby to make gain to the Estate.* * * * (Italics supplied.)

The "Articles of Administration" provided for limited liability of the "trustees." It provided that the "trustees" were to keep records and make ther financial reports annually. They were also to allot in the

records "expectancy fractions" under instructions to be delivered by Norman Lombard, one of the "trustees." The "trustees" were enjoined to refrain from any actual or pretended issue or sale of capital stock in or of their Estate, such being a corporation prerogative and they were also prohibited from issuing or selling any equities or beneficial or equitable interest in the Estate. (R. 57–58.) It was provided, however, that "Dormant fractions, their usefulness being contingent upon possible future convenience, remain subject to the discretion of the Trustees." (R. 33.) The "Articles" provide further that "it is advisable to elect presiding officer and select and appoint a Board Secretary and/or other officials, to delegate duties and authority"; the trustees shall fix and pay all compensation to officers, agents and employees and in their discretion pay themselves "reasonable" compensation. (R. 29.)

Nowhere in the "Hulbert Plan" which was executed is there a conveyance to trustees for the benefit of *cestuis que* trust. Although the "Plan" contemplated that expectancy fractions" should be "allotted as to beneficiaries," as a matter of record only, in a "Register," it is provided that such allocation shall be a "guide" to enable the "trustees" to properly "apportion each distribution." The matter of allotting "expectancy fractions" meant no more than making a record of who was entitled to receive distributions and the proportion each would receive, if, as, and when any distributions were ever made, which was entirely within the discretion of the "trustees." (R. 58.) Death of a beneficiary would not entitle the heirs to demand a portion or distribution of "Estate" funds, but legal heirs

may succeed to the expectancy. A beneficiary is defined as "One Who Tenants Property, subject to and without affecting the discretion, management and/or absolute ownership of the Trustees in whom legal and equitable title to all Estate properties are Vested." (R. 33.)

The transfers of property to "trustees" were irrevocable, and they were to hold the property until they decided to liquidate, but the longest period was fixed, so as not to violate the rule against perpetuities, by the life of the last surviving subscriber to the agreement or registered "beneficiary." (R. 59–60.)

The third instrument, constituting a part of the "Hulbert Plan," was the direction from Norman Lombard to the "Board of Trustees" to register Charles S. Lombard as a "beneficiary" and to allocate to him 600 "expectancy fractions" out of a total of 1,200, leaving 600 dormant "expectancy fractions." (R. 59.)

The persons registered as having "expectancy fractions" could, however, be changed. On February 10, 1937, Dr. Lombard requested in writing that the board of trustees of taxpayer vacate the registration of the 600 "expectancy fractions" in his name and reallocate and re-register them so that 350 fractions be re-registered in the name of himself and Bertha Lombard as joint tenants, and that 50 fractions each be registered in the names of Norman, Winthrop, Emily and Ruth Lombard and Dorothy Pray. At a meeting of the board of trustees on March 14, 1937, the request was approved by resolution and the secretary was directed to register the new beneficiaries in accordance with the request. The resolution stated that the board of

trustees approved "the registrations as of the date of the Request, February 10, 1937." The registrations were made in the register on March 14, 1937. The re-registrations in the names of the various beneficiaries were made without consideration. On February 25, 1938, Dr. and Mrs. Lombard requested the taxpayer's board to vacate the "expectancy fractions" registered in their names and re-register them as follows: Two hundred to themselves as joint tenants and 50 each to George S. Lombard, Charles S. Lombard, jr. and Lillis S. Stowe. At a meeting of the "trustees" on February 26, 1938, a resolution was adopted approving the request and the re-registrations were made in accordance therewith. No other re-allocations nor re-registrations have been made. (R. 60–61.)

Dr. Lombard filed a gift tax return for 1935 in which he reported transfers of property to Lombard Trustees, Ltd., with values as follows (R. 61):

November 3, 1935, real property, Redlands	$5, 610. 00
November 19, 1935, real property, lot, Redlands	24, 190. 00
November 19, 1935, real property, lot and building, Redlands	17, 540. 00
November 19, 1935, real property lots	13, 830. 00
November 19, 1935, real property, lot and filling station Riverside	810. 00
November 19, 1935, real property, 4 lots, San Diego	2, 500. 00
November 19, 1935, real property, orange grove Redlands	2, 000. 00
December 31, 1935, stocks	64, 587. 93
	$131, 067. 93

Several of the pieces of real estate conveyed to the taxpayer are business properties, stores and offices, which are rented. In 1937 these business properties and the orange grove produced income which was reported by the taxpayer on Form 1041, "Fiduciary Income Tax Return," as follows (R. 62):

Dividends	$4,234.95
Interest on bank deposits	200.00
Rents—net—after repairs, depreciation and expenses	14,230.05
Receipts from orange grove—net—proceeds from sale of oranges	10,048.12
Total	$28,713.72

The taxpayer in the aforesaid fiduciary income tax return reported net income after deductions in the amount of $23,014.05. Among the deductions taken were the following: Interest paid on note for $39,000, $2,052.52; city and county taxes on property, $155.92; state income tax, $137.50; social security tax, $14.94; miscellaneous expenses, $425.68; salaries, $2,904.84. Attached to the fiduciary income tax return was Form 1040 F, "Schedule of Farm Income and Expenses." On this return the taxpayer reported $24,634.95 from the sale of oranges and $494.66 from receipts from "water and pipeline," and miscellaneous, and total ex-
receipts of $10,048.12. The expenses of operating the orange
penses of $15,081.49, leaving net grove included wages, fertilizers, spraying materials, fuel, taxes, insurance, water rent, smudge oil, tractoring, telephone and repairs. (R. 62–63.)

Taxpayer reported in the fiduciary income tax return as distributable income of the registered beneficiaries total net income for 1937 as follows:

Norma Lombard	$1,917.84
Emily Lombard	1,917.84
Ruth Lombard	1,917.84
Winthrop Lombard	1,917.84
George Lombard	1,917.84
Charles S. Lombard	5,753.51
Bertha Lombard	5,753.50
Dorothy Pray	1,917.84
	$23,014.05

On January 1, 1937, there was on the orange grove a matured crop of navel oranges. On February 23,

1937, the navel orange crop was sold for the sum of $2.80 per hundred pounds on the trees. The buyer was to pick and haul, and the picking was to begin March 1, 1937, and to be completed by April 10, 1937. The crop was picked by the buyer between March 1, 1937, and April 13, 1937. No expense was incurred or paid by the "trustees" in connection with the crop after its sale on February 23, 1937. The following amounts were received by the taxpayer for the crop: February 23, 1937, $10,000; March 10, 1937, $5,000; April 15, 1937, $1,868.96. In determining the net income for different periods in 1937 above, each payment received for the oranges was credited to gross income for the period in which received. (R. 63–64.)

The only sales made by the "trustees" apart from ranch products after March 14, 1937, were the following: March 24, 1937, stock of American Trust Company costing $5,189.44 was sold for $5,145.35 and stock of Baltimore American Insurance Company was purchased for $5,133.75; on July 13, 1938, bonds of Kansas City School were sold for $5,520.75. (R. 64.)

On June 14, 1940, which was prior to the mailing of the notice of deficiency herein, the taxpayer mailed to the Collector of Internal Revenue, Los Angeles, a duly executed capital stock tax return on Form 707 for the year ending June 30, 1937, wherein the value of the taxpayer's "capital stock" was declared to be $150,000. The taxpayer enclosed a check in the amount of $213.75 for the payment of the capital stock tax of $150, a 25-percent penalty for delinquency, $37.50 and interest from August 1, 1937, $26.25. The amount so paid has

never been refunded to the taxpayer and no claim for refund has been filed or made. (R. 64.)

The taxpayer's adjusted net income for the entire calendar year 1937 was $22,902.04, of which $4,234.95 was from dividends. (R. 64.)

A trust at law was not created by Dr. Lombard by his execution on November 3, 1935, of the several instruments constituting the Hulbert Plan, and taxpayer was not a trust prior to or during the taxable year. Rather, some type of enterprise in the nature of a family corporation was created under the Hulbert Plan. Dr. Lombard transferred absolute title, legal and equitable, to various properties, real and personal, to himself, Norman Lombard, and Bertha Lombard, as joint tenants. They, and they only, were the equitable as well as the legal owners of the property. They and their successors, only, could determine who should eventually receive distribution of the property upon liquidation of the enterprise. (R. 65.)

On the basis of the foregoing facts the Board of Tax Appeals affirmed the Commissioner's determination (R. 1–2) based on his amended answer at the hearing before the Board (R. 3), in which it was claimed that the taxpayer was an association taxable as a corporation during the entire year of 1937 (R. 65-73). The Board thereupon entered its decision (R. 74) from which the taxpayer petitioned this Court for review (R. 75–77).

SUMMARY OF ARGUMENT

The taxpayer was taxable at corporate rates throughout 1937. This Court in *Porter* v. *Commissioner,* 130 F. 2d 276, consistent with all the authorities, stated the

test of treating a nonincorporated organization as a corportation as first, and more important, it must have a business purpose, and second, it must have business activity. The Board of Tax Appeals found both factors. These findings are supported by substantial evidence and may not therefore be disturbed on review. Moreover, the instruments on the basis of which this Court affirmed the Board's finding of a business purpose in the *Porter* case are identical with the ones here involved. The Board correctly refused to consider evidence outside the "trust" instruments in ascertaining the purpose of the taxpayer.

The fact that Dr. Lombard was the sole registrant of expectancy fractions until March 14, 1937, requires no different conclusion as to taxpayer's status prior to that date. Three or more "associates" existed at all times in the form of trustees, who unlike the trustees in the ordinary trust, had absolute ownership of the property. Moreover, it was contemplated at the outset that the organization was to be utilized to bring in additional registrants of participating fractions. In either view there were "associates". But if form is of any importance, it is, only to the extent that the tax result changes as an organization looks more or less like a corporation. And corporations with but one stockholder or one beneficial owner are common. The taxpayer had all of the features of a corporation except incorporation—separate entity, trade name, seal, limited liability, transferable interests, centralized management and continuity. The "association" concept was designed only as a catch-all for "business-purpose" en-

tities short of incorporation. Nothing turns on how close a taxpayer approaches the notion of association in the abstract. If it has a business purpose and business activity and is an entity distinct from an individual so as to secure the advantages of the corporate form, it is taxable as a corporation.

Counsel's argument, that the income of the trust from January 1 to March 14 of the taxable year is taxable to Dr. Lombard, under Section 166 of the Revenue Act of 1936, as grantor of a revocable trust, is untenable. Whether a business trust is revocable or not, Section 1001 (2) is applicable to tax the income to the trust and no provision is made for taxing income of business trusts to grantors where they, or persons not having substantially adverse interests, have the power of revocation. This position is confirmed by a consideration of the statutory plan which has always made a distinction of the most fundamental nature between corporate income on the one hand, and individual or trust income, on the other. In the case of traditional trusts income is taxable either to the grantor, beneficiaries or fiduciary, but in the case of corporations the act makes no provision except to tax income to the entity. Thus when it is established that the income of a trust is to be taxed as a corporation pursuant to Section 1001 (2), the income must necessarily be taxed to the trust. There are no provisions for doing otherwise. To say that the income is taxable to the grantor under Section 166 requires that it first be established that a traditional trust is involved rather than a business type.

ARGUMENT

The taxpayer, Lombard Trustees, Ltd., was an association taxable as a corporation during all of 1937

(a) The taxpayer was organized for a business purpose and engaged in continuing business activity during the entire taxable year

The Board of Tax Appeals found that the taxpayer, Lombard Trustees, Ltd., was organized for the purpose of putting all of Dr. Lombard's business properties under centralized and continuous management for realizing profits and distributing them to all who came into the plan and that it was a business enterprise whose activities included renting several properties, managing buildings and growing oranges. (R. 71.) On the basis of these and other findings of fact, it held that the taxpayer was an association and therefore taxable as a corporation during the entire taxable year 1937 (R. 73) pursuant to Section 1001 (a) (2) of the Revenue Act of 1936 which provides that "When used in this act * * * The term 'corporation' includes associations."

The taxpayer was created by the use of copyrighted forms called the "Hulbert Plan". (R. 65.) It was these identical forms which were involved in *Porter* v. *Commissioner,*[1] 130 F. 2d 276, affirming *Porter Property Trustees, Ltd.* v. *Commissioner,* 42 B. T. A. 681, in which this Court decided that the taxpayer was an association taxable as a trust. This Court there said (p. 279):

> There are two tests to be applied to a trust in order to determine whether or not it is taxable as a corporation: (1) What is its purpose?; and

[1] The findings below make this clear, 42 B. T. A. 681, 690.

(2) what is the extent of its business activity? Of the two, the first is the more important. * * *

The Board's finding of a business purpose was based on the general purpose stated in the "Plan", the broad powers given to the taxpayer and its business activities. It is submitted that this finding is fully supported by substantial evidence and is therefore binding on this Court. *Phillips* v. *Commissioner,* 283 U. S. 589, 600; *Helvering* v. *Rankin,* 295 U. S. 123, 131. It would seem unnecessary to review the provisions of the documents by which taxpayer was established since it is apparent from a comparison of the statement, *supra,* with the findings of the Board of Tax Appeals in the *Porter* case, *supra,* that the documents were identical except for differences in names. Since the documents are identical the remarks of this Court in *Porter* v. *Commissioner,* 130 F. 2d 276, concerning the intention expressed therein apply with equal force here (p. 280):

> There is here no expressed purpose of liquidation, or of conservation, but an avowed intent "to engage in any lawful business" in order to realize a gain or profit to the trust estate. Here is continuity of existence and operations "during any lawful term" despite any change in beneficiaries. Clearly, then the trust instrument exhibits authority in the trustees to engage in business. * * *

The taxpayer's counsel concede the soundness of the *Porter* decision (Br. 5), but argue that the instant case is distinguishable because in the *Porter* case "there was no specific evidence of purpose" (Br. 38). It appears from the context that by this statement they apparently

mean that there was in the *Porter* case no source from which intention could be ascertained other than the "trust" documents. (Br. 32–38.) Counsel urge that an amendment of the "trust" instruments made September 30, 1938 (R. 70) and a stipulation as to Dr. Lombard's testimony concerning his intention [2] (Br. 34) be considered on this issue. The amendment was obviously not material in determining the purpose of the 1935 instrument in effect in 1937. Moreover, it would not be proper to consider it or Dr. Lombard's testimony as indicative of the purpose of the "trust" in 1937 as the Board properly refused to do on the authority of *Helvering* v. *Coleman-Gilbert,* 296 U. S. 369. While it is not clear that counsel are correct in asserting that there was no evidence in the *Porter* case other than the "trust" instrument to ascertain the purpose of the arrangement, the following statement from this Court's opinion makes it clear that if there had been the Court would have refused to consider it (p. 279):

> The Supreme Court also said, in the *Morrissey* case, 296 U. S. at page 361, 56 S. Ct. at page 296, 80 L. Ed. 263, that the character of the enterprise was "determined by the terms of the trust instrument." In *Helvering* v. *Coleman-Gilbert Associates,* 296 U. S. 369, 373, 56 S. Ct. 285, 287, 80 L. Ed. 278, decided the same day as the *Morrissey* case, the Supreme Court expressed the thought as follows: "* * * Weight should be given to the purpose for which the

[2] Exhibit 2 (R. 15–19) is "Stipulation B". It states what Dr. Lombard would testify if permitted to over the Commissioner's objection. It is also stipulated that this exhibit was admitted in evidence at the hearing. (R. 3.)

> trust was organized, but that purpose is found in the agreement of the parties. Not only were they actually engaged, as the Board of Tax Appeals determined, in carrying on an extensive business for profit, but the terms of the trust instrument authorized a wide range of activities in the purchase, improvement and sale of properties in the cities and towns of the state. *The parties are not at liberty to say that their purpose was other or narrower than that which they formally set forth in the instrument under which their activities were conducted.* [Emphasis supplied by the Court.]

Counsel cite no authority for their proposition that the purpose of the trust may be ascertained apart from the trust instrument (Br. 32–38), but argue that *Helvering* v. *Coleman-Gilbert, supra,* is consistent with the interpretation that an oral agreement might be considered. They refer to the language of the Court that (p. 279) "Weight should be given to the purpose for which the trust was organized, but that purpose is found in the agreement of the parties", and argue that the Court did not insert "written" before agreement. (Br. 33.) But as this Court noted in the italicized portion of its opinion quoted above from the *Porter* case, the Supreme Court expressly stated in the same paragraph from which counsel quote that the purpose set forth in the *instrument* was conclusive. And, Article 1001–3 of Treasury Regulations 94 (Appendix, *infra*) states that "The purpose will not be considered narrower than that which is formally set forth in the instrument under which the activities of the trust are conducted." It is thus apparent that the Board was

correct in rejecting evidence of purpose other than as found in the "trust" instrument.

Applying the second test in the *Porter* case—the extent of the business activity—the Board concluded that the taxpayer's activities in the taxable year included the renting and managing of various business properties and growing oranges. (R. 71.) The Board stated (R. 71):

> From the limited facts on the point, it appears that petitioner is a business enterprise. It rents several properties and manages the buildings. The net annual rents, without considering depreciation, amount to $15,751.10. The properties include four "mercantile buildings", a store, and a service station with equipment. Petitioner grows oranges, which is certainly an agricultural and business enterprise. In this activity petitioner expended for "farm expenses" over $14,000. In 1937 the orange crop was sold for a gross amount of $24,635.

These findings are amply supported by the record. It appears from the gift tax return [3] filed by Dr. Lombard in 1935 that the following property was transferred to the "trust" during 1935 (R. 61):

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[3] It was stipulated that this return and the taxpayer's fiduciary return for 1937 were offered and received in evidence (R. 3), and the taxpayer designated the entire transcript to be printed as the record (R. 78–79). These returns were not, however, printed as a part of the record, but the Board's findings include the necessary information taken from them. The taxpayer apparently makes no objections to the accuracy of the Board's findings in this respect and this accuracy is readily verified by resort to the original record.

November 3, 1935, real property, Redlands	$5,610.00
November 19, 1935, real property, lot, Redlands	24,190.00
Novemger 19, 1935, real property, lot and building, Redlands	17,540.00
November 19, 1935, real property, lots	13,830.00
November 19, 1935, real property, lot and filling station Riverside	810.00
November 19, 1935, real property, 4 lots, San Diego	2,500.00
November 19, 1935, real property, orange grove, Redlands	2,000.00
December 31, 1935, stocks	64,587.93
	$131,067.93

It is to be assumed, since nothing appears to the contrary, that the "taxpayer" retained this property in 1937. The fiduciary return filed by the taxpayer in 1937 indicated income as follows (R. 62):

Dividends	$4,234.95
Interest on bank deposits	200.00
Rents—net—after repairs, depreciation and expenses	14,230.65
Receipts from orange grove—net—proceeds from sale of oranges	10,048.12
Total	$28,713.72

The fiduciary return showed deductions as follows (R. 62): Interest paid on a note for $39,000, $2,025.52; city and county property taxes, $155.92; state income tax, $137.50; social security tax, $14.94; miscellaneous expenses, $425.68; salaries, $2,904.84. Form 1040 F, "Schedule of Farm Income and Expenses" attached to the fiduciary return showed (R. 62) $24,634.95 from the sale of oranges and $494.66 from receipts from "water and pipeline"; total expenses of $15,081.49; net receipts of $10,048.12. The expenses of operating the orange grove includes wages, fertilizers and spraying materials, fuel, taxes, insurance, water rent, smudge oil, tractoring, telephone and repairs. (R. 62–63.) Apart from ranch products the sales made after March 14, 1937, were on March 24, 1937, when stock of American Trust Company costing $5,189.44 was sold for $5.145.35 and on

July 13, 1938, bonds of Kansas City School were sold for $5,520.75. On March 24 stock of Baltimore American Insurance Company was purchased for $5,133.75. (R. 64.) It is submitted that this evidence of business activity which includes extensive managing of property, operating an orange grove and, to a limited extent, buying and selling securities is sufficient business activity to warrant taxing the taxpayer as a corporation.[4] *Porter* v. *Commissioner, supra.* There, after finding in the identical instrument involved here a purpose to engage in business as noted *supra,* it was stated (p. 280):

> The activities of the trustees do not compel a contrary conclusion, but give rise to the conclusion that the activities during the taxable year were sufficent to constitute carrying on business. *Flint* v. *Stone Tracy Co.,* 220 U. S. 107, 171, 31 S. Ct. 342, 55 L. Ed. 389, Ann. Cas. 1912B, 1312; *Von Baumbach* v. *Sargent Land Co.,* 242 U. S. 503, 514, 515, 37 S. Ct. 201, 61 L. Ed. 460; *Hecht* v. *Malley,* 265 U. S. 144, 161, 162, 44 S. Ct. 462,

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[4] Taxpayer complains (Br. 31):

> It does appear, however, that during the 4 years and 3 months that elapsed between March 14, 1937 and the hearing, the trustees made only two sales apart from ranch products, and sold only one small block of stock and one small block of bonds. [T. 15.] This is some evidence of inactivity and lack of profit purpose. It shows that the trustees were engaging only in the business of managing the properties received from Dr. Lombard. The Board fails to note such inactivity and its significance, while drawing an unwarranted inference from the fact that the trustees managed the property received from Dr. Lombard.

This contention would have merit if the only business were that of buying and selling securities. But it completely overlooks the ranching and real estate activities.

68 L. Ed. 949; *Thrash Lease Trust* v. *Commissioner,* 9 Cir., 99 F. 2d 925, 928. The activities here "went beyond transactions carried on for the single purpose of effecting a liquidation of assets; * * *." *Willis et al.* v. *Commissioner,* 9 Cir., 58 F. 2d 121, 123. Cf. *United States* v. *Rayburn,* 8 Cir., 91 F. 2d 162, 167, 168. Moreover, it is not alone what the trustees did during the taxable year, but what they were empowered to do. *Morrissey* v. *Commissioner,* 296 U. S. 344, 361, 56 S. Ct. 289, 80 L. Ed. 263; *Commissioner* v. *Vandegrift Realty & Investment Co.,* 9 Cir., 82 F. 2d 387, 390; *Sloan* v. *Commissioner,* 9 Cir., 63 F. 2d 666, 669, 670. Cf. *Helvering* v. *Washburn,* 8 Cir., 99 F. 2d 478, 481.

As pointed out *supra,* in addition to the business activities actually engaged in the taxpayer had the authority as in the *Porter* case to "own real estate or personal property in any State without limit, may buy, sell, improve, exchange, assign, convey and deliver, may grant trust deeds and may mortgage or otherwise encumber for obligations; may own stock in or entire charters of corporations, and may engage the Estate funds and properties in any industry or investment in their discretion, hoping thereby to make gain to the Estate." (R. 27–28.) It is no longer open to question that any activities which amount to more than a mere passive holding of property and a receipt of income therefrom are sufficient to constitute the carrying on of a business. *Morrissey* v. *Commissioner,* 296 U. S. 344; *Helvering* v. *Coleman-Gilbert, supra; Swanson* v. *Commissioner,* 296 U. S. 362; *Helvering* v. *Combs,* 296 U. S. 365; *Hecht* v. *Malley,* 265 U. S. 144; Treasury

Regulations 94, Art. 1001–2 and 1001–3. In the case at bar, the purposes in the formation of the "trust" as well as the activities carried on amounted to much more than mere protection, conservation, and distribution of property. Even where the trustees' sole functions in connection with the oil produced from the trust's oil leases were to collect, care for, and dispose of the oil, this Court held such activities constituted doing business for profit so that the trust was taxable as a corporation. *United States* v. *Trust No. B. I. 35, Etc.,* 107 F. 2d 22 (C. C. A. 9th), reversing 25 F. Supp. 608 (S. D. Cal.). And in *Marshall's Heirs* v. *Commissioner,* 111 F. 2d 935 (C. C. A. 3d), certiorari denied, 311 U. S. 658, it was held a sufficient business activity to constitute the trust an association taxable as a corporation where the trust was formed merely to manage property owned by four heirs and leased to others.

(b) The fact that expectancy fractions were registered in Dr. Lombard's name only prior to March 14, 1937, does not affect taxpayer's status as an association

Taxpayer's counsel argue that assuming the taxpayer was taxable as a corporation subsequent to March 14, 1937, it was not taxable as such prior to that time. They contend that since prior to March 14, 1937, Dr. Lombard was the sole beneficiary of the "trust" there were no "associates" and thus there was no association which could be taxed as a corporation. (Br. 5–15.)

The taxpayer was formed when Dr. and Mrs. Lombard, as grantors, executed the "Hulbert Plan Trust" naming Winthrop, Emily, and Norman Lombard as trustees (R. 55) and when Norman Lombard named

the owners of the "expectancy fractions" in a separate instrument (R. 59). He directed that Dr. Lombard be allocated 600 of a total of 1200 "expectancy fractions". Emily and Winthrop Lombard resigned as trustees and were succeeded by Dr. and Mrs. Lombard. Thus at the outset there were five individuals involved in the organization—two grantors and three trustees and no beneficiaries. The situation on the same day was changed so that there remained two grantors who, together with one other, were the trustees and in one of the grantors' names half of the expectancy fractions were issued; the other half "remain subject to the discretion of the Trustees." (R. 33.) At all times, therefore, there were at least three separate persons connected with the enterprise. If "associates" are necessary, were these three "associates" from January 1, 1937, to March 14, 1937? A clear answer in the affirmative is furnished by *Hecht* v. *Malley,* 265 U. S. 144, which modified *Crocker* v. *Malley,* 249 U. S. 223, and resulted in the final step in the logical development of the association doctrine taken in *Morrissey* v. *Commissioner, supra.* The Court, in holding a "Massachusetts Trust" an association taxable as a corporation, said, after defining "association" in its "ordinary meaning" as a "body of persons united without a charter, but upon the methods and forms used by incorporated bodies" (pp. 157, 161):

> We think that the word "association" as used in the Act clearly includes "Massachusetts Trusts" such as those herein involved, having quasi-corporate organizations under which they

> are engaged in carrying on business enterprises. * * *
>
> * * * * *
>
> We conclude, therefore, that when the nature of the three trusts here involved is considered, as the *petitioners are not merely trustees* for collecting funds and paying them over, *but are associated together in much the same manner as the directors in a corporation for the purpose of carrying on business enterprises,* the trusts are to be deemed associations within the meaning of the Act of 1918; * * *. [Italics supplied.]

This case has been cited with approval in almost all subsequent association cases and no case was found in which disapproval was shown either of its language or result.

Morrissey v. *Commissioner, supra,* extended to income tax the doctrine of the *Hecht* case which was concerned with a capital stock tax. There the Court said (p. 357):

> Thus a trust may be created as a *convenient method by which persons become associated* for dealings in * * * [the Court lists specific businesses] or other sorts of business; *where those who become beneficially interested, either by joining in the plan at the outset, or by later participation according to the terms of the arrangement, seek to share the advantages of a union of their interests in the common enterprise.* [Italics supplied.]

Thus, while it appears that in the *Morrissey* case the the Court speaks of the associates in terms of beneficiaries, it emphasizes that the entity is an association regardless of whether the beneficiaries come into the enterprise at the outset or come in later according to

the terms of the arrangement. See *Second Carey Trust* v. *Helvering,* 126 F. 2d 526, 528 (App. D. C.), certiorari denied, October 12, 1942. These cases describe precisely the situation in the case at bar as evidenced by the Board's findings that (R. 69):

> Dr. Lombard set about to obtain the consent of eight of the children to come into the plan. He did not obtain their consent at first and for that reason the entire 600 "issued" units of interests were registered in his name. The reregistrations of the 600 units to register interests in various children which were made on March 14, 1937, and February 26, 1938, were made pursuant to the consent of the eight children at or about such dates to come into the plan.

These findings are amply supported by the record. (R. 10–11, 15–19, 38–39, 40–41.)[5] Indeed, counsel concede that such was the situation (Br. 14):

> It may be conceded that at the time the trust declaration was executed in November, 1935, Dr. Lombard did intend or propose that *ultimately* the beneficial interest under the trust would be held by the members of his family and himself. * * *

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[5] These findings are based partially on Stipulation B referred to in footnote 2, *supra.* Counsel object to the use of Dr. Lombard's testimony on the issue of the number of beneficiaries contemplated when the Board rejected it on the issue of purpose. As argued, *supra,* the Board was correct in so rejecting the extraneous evidence of purpose, but there appears no reason for excluding evidence relevant to a determination of who the intended beneficiaries were. In any event, as the record references indicate, and on the basis of counsel's concession, noted *supra,* the conclusion is supported by the provision of the "trust" instrument and what was done pursuant thereto without resort to Dr. Lombard's testimony.

Counsel's preoccupation with the number of beneficiaries goes to a question of form which the cases and the Regulations (Appendix, *infra*) have consistently stated is of no importance. *Morrissey* v. *Commissioner, supra*; *Commissioner* v. *Vandegrift Realty & Investment Co.,* 82 F. 2d 387 (C. C. A. 9th). This was properly recognized in *Porter* v. *Commissioner, supra,* when, as noted *supra,* this Court stated that the two tests of taxability as a corporation are (1) the purpose of the organization, and (2) the extent of its business activity. The Supreme Court in the *Morrissey* case gave some weight to the features of a trust that make it enough like a corporation when it is organized as, and carrying on, a business to require that it be taxed as a corporation. These features it described as follows (p. 359):

> What, then, are the salient features of a trust—when created and maintained as a medium for the carrying on of a business enterprise and sharing its gains—which may be regarded as making it analogous to a corporate organization? A corporation, as an entity, holds the title to the property embarked in the corporate undertaking. Trustees, as a continuing body with provision for succession, may afford a corresponding advantage during the existence of the trust. Corporate organization furnishes the opportunity for a centralized management through representatives of the members of the corporation. The designation of trustees, who are charged with the conduct of an enterprise, who act "in much the same manner as di-

> rectors," may provide a similar scheme, with corresponding effectiveness. Whether the trustees are named in the trust instrument with power to select successors, so as to constitute a self-perpetuating body, or are selected by, or with the advice of, those beneficially interested in the undertaking, centralization of management analogous to that of corporate activities may be achieved. An enterprise carried on by means of a trust may be secure from termination or interruption by the death of owners or beneficial interests and in this respect their interests are distinguished from those of partners and are akin to the interest of members of a corporation. And the trust type of organization facilitates, as does corporate organization, the transfer of beneficial interests without affecting the continuity of the enterprise, and also the introduction of large numbers of participants. The trust method also permits the limitation of the personal liability of participants to the property embarked in the undertaking.

The taxpayer has every corporate feature there designated. (1) Taxpayer holds legal and equitable title to the property. (R. 30.) (2) It has a continuing body of trustees with provisions for succession. (R. 25–26.) (3) It provides the opportunity of centralized management. (R. 20, 25–26, 27–28, 29, 30.) (4) The trustees are charged with the management of the enterprise. (R. 25.) (5) The trustees are named in the trust instrument. (R. 23–24.) (6) The death of beneficial owners does not terminate or interrupt the organization. (R. 33.) (7) Beneficial interests can be

transferred without affecting the continuity of the enterprise. (R. 39.) (8) Liability is limited. (R. 30-31.)

The "trust" instruments in at least seven separate paragraphs state that the legal and equitable interest in the property conveyed is in the trustees. (R. 20, 22, 24, 25, 30, 33.) It is commonplace that a trust is a device whereby legal interest in property is held by one or more persons for the benefit of one or more persons who have the equitable title. Restatement of the Law of Trusts, Sec. 2; Scott, The Nature of the Rights of the Cestui Que Trust, 17 Col. L. Rev. 269. Thus the Restatement states (p. 10):

> In a trust there is a separation of interest in the subject matter of the trust, the beneficiary having an equitable interest and the trustee having an interest which is normally a legal interest.

It may be noted that this is the rule in California (cf. *Title Ins. & Trust Co.* v. *Duffill,* 191 Cal. 629; *Keeney* v. *Bank of Italy,* 33 Cal. App. 515; cf. also California Annotations to the Restatement of the Law of Trusts, Sec. 2), although according to the Regulations, local law is of no importance in connection with this section. Regulations 94, Art. 1001–1 (Appendix, *infra*). It is likewise commonplace that the intention as expressed in the instrument must control the type of interests created. *Title Ins. & Trust Co.* v. *Duffill, supra.* It must be concluded that the taxpayer was more like a corporation than most ordinary business trusts which are taxed as corporations.

Unquestionably the purpose of Congress in taxing associations as corporations was to provide the same tax rate for entities which are not technically corporations but which carry on a business with all the advantages of the corporate form. Thus Article 1001–2 of Treasury Regulations 94 (Appendix, *infra*) states:

> The term "association" is not used in the Act in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by a single individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an "investment" trust (whether of the fixed or the management type), an interinsurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Act, a trust or an estate, or a partnership. If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

Here is an organization which lacks only a charter to be a corporation, for corporations with but one stock-

holder are common.[6] Thus the corporation sole while not frequently observed still exists. Fletcher, Cyclopedia Corporations, Sec. 50, p. 184. And aggregate corporations organized and owned by one individual are common phenomena. Cf. for example, *Menihan* v. *Commissioner,* 79 F. 2d 304 (C. C. A. 2d); *Burnet* v. *Commonwealth Imp. Co.,* 287 U. S. 415; *Higgins* v. *Smith,* 308 U. S. 473; *Werner* v. *Hearst,* 177 N. Y. 63; *Louisville Gas & Electric Co.* v. *Moore,* 215 Ky. 273; *Button* v. *Hoffman,* 61 Wis. 20.

Since the purpose of taxing "associations" as corporations is to provide the same tax rate to organizations which do business with the advantages of the corporate form without being technically a corporation, the inquiry must be directed toward the concept "corporation" rather than "association." "Association" is merely a generic term under which all such noncorporate entities are grouped for convenience of definition. To approach the problem in the narrowly conceptualistic manner of the taxpayer is to invite incongruity and uneven application of the revenue act. Even if counsel's contention is sound that taxpayer is not technically an "association" because it lacks associates, it nevertheless cannot be denied that it is more like a corporation than most entities which have been classified as association and accordingly taxed as a corporation. Yet the test of taxability as a corporation is

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[6] It requires no citation of authority to establish that "Massachusetts Trusts" which Regulations 94, Article 1001–2 expressly provides are taxable as corporations need have only one beneficiary.

similarity to it. The incongruity can only be resolved by a pragmatic application of the association concept. That is the clear import of the statute, regulations and decisions.

Nor do counsel's authorities establish the contrary. His reliance on Section 19.3797 of Regulations 103 is misplaced. (Br. 10–11.) Regulations 94, Articles 1001–1, 1001–2 and 1001–3, were adopted pursuant to the Revenue Act of 1936 and are controlling here. When those articles (which are substantially like those relied upon by counsel) are read in their entirety rather than taking excerpts as counsel have done, it is clear that they support in all respects our contention here. The language which the taxpayer emphasizes comes from the section which is entitled "Trust Distinguished from Association." The section differentiates between a trust with more than one beneficiary and an association with more than one, probably because that is the more usual situation. Nowhere does the article make plurality of beneficiaries a *sine qua non* of association. Indeed, to do so would be utterly inconsistent with the admonition in Article 1001–1 that technical distinctions are of no importance and the tests of the regulations and cases which are business purpose and business activity. Counsel cite *McKean* v. *Scofield,* 108 F. 2d 764 (C. C. A. 5th); *U. S. Trust Co.* v. *Commissioner,* 296 U. S. 481; and *Magoon Trust Estate* v. *Commissioner,* decided July 10, 1942 (Prentice Hall B. T. A. Memo. Service, pars. 42,406, 43,406–A). These cases all involved the question of whether separate trusts with either common trustees or beneficiaries should be taxed as one

entity. They, therefore, obviously have no relation to the issue on which they were cited. It may be noted also that taxpayer's quotations from *Morrissey* v. *Commissioner, supra; Helvering* v. *Coleman-Gilbert, supra,* and *Cleveland Trust Co.* v. *Commissioner,* 115 F. 2d 481 (C. C. A. 6th) (Br. 9), while defining associations in terms of associates nowhere state that the beneficiaries rather than all the parties to the organization must be considered the associates.

(c) Section 166 of the Revenue Act of 1936 is not applicable here and the income of the taxpayer prior to March 14, 1937, was therefore not taxable to Dr. Lombard

The taxpayer's second major contention against its being taxed as a corporation from January 1, 1937, through March 14, 1937, even if it is taxable as such subsequent to March 14, is that under Section 166 of the Revenue Act of 1936 (Appendix, *infra*) the income during that period is taxable to Dr. Lombard as grantor. There is an insurmountable obstacle to this contention. Section 166 has no application to an entity which is classified as a corporation.

Under Sections 161 and 162 of the Revenue Act of 1936 the income of estates and trusts is required to be determined, with exceptions that are not material, as in the case of individuals and is made subject to the taxes imposed on individuals by Sections 11 and 12. Section 162 (b) and (c) allows deductions to trusts to the extent that income is to be distributed currently to the beneficiaries, or that income is properly paid or credited to them in the discretion of the trustees and requires the beneficiaries to report these amounts as income. Sections 166 and 167 provide that under cer-

tain circumstances the grantor may be taxed. Thus the statute taxes trust income at *individual rates* either to the grantor,[7] to the fiduciary (trust) or to the beneficiaries depending on the circumstances.

Under the Revenue Act of 1936 and the preceding acts, however, a corporation is allowed different credits and deductions than are allowed to individuals and is subjected to different taxes. Thus Section 13 of the Revenue Act of 1936 provides a relatively level graduated normal tax on corporations and an entirely new theory of taxation is embodied in Section 14 in the form of a steeply graduated surtax on undistributed profits of corporations. The normal tax on individuals (Sec. 11 of the Revenue Act of 1936) and the surtax on individuals (Sec. 12) provide an entirely different pattern. As established under (a) and (b) *supra,* whether the taxpayer is taxable as a corporation is made dependent solely on whether it is to be classified as a corporation. Section 1001 (2) of the Revenue Act of 1936. Once it is established that an entity is to be classified as a corporation it must be taxed under Sections 13 and 14, which are in terms applicable to "every corporation" (Sections 13 (b) and 14 (b)), and the provisions relating to trusts are no longer applicable. This is so obvious that it has long been taken

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[7] Regulations 94, Art. 166–1 provides: "If the grantor of a trust is regarded, within the meaning of the Act, as remaining in substance the owner of the corpus thereof, the income therefrom is not taxable in accordance with the provisions of sections 161, 162, and 163 but remains attributable and taxable to the grantor". It is therefore the unmistakable implication that taxation pursuant to Section 166 is at individual rates as is the case of Section 166 and the tax is levied pursuant to Sections 11 and 12.

for granted by the courts. The statute contains no exceptions under which a business trust may be taxed under Sections 162 or 166 rather than under Sections 13 and 14. The taxpayer's argument merely amounts to dressing up the point of view which is usually urged and rejected for taxing a business entity as a fiduciary under Section 162 and hence at individual rates under Section 11. For his argument resolves itself into contending that even though taxpayer is a business entity, individual rates should apply. The only refinement in this argument is the new twist—a revocable corporation! But income of business entities, whether or not "revocable" are taxed to the *organization* at corporate rates under Sections 13 and 14. No alternative is available.[8] Section 1001 (2) operates with the same effect to tax business-purpose trusts which are revocable and thereby excludes resort to Section 166 which is concerned with non-business trusts as it does in the case of non-revocable trusts to the exclusion of Section 162.

Thus the taxpayer was taxable at corporate rates thoughout 1937 because it was organized for business purposes and was engaged in business during the entire year. It was in form a corporation except for formal incorporation. It had "associates" but even if it did not it would be a distinction upon which no tax result turns. And finally, the income is not taxable to Dr. Lombard because Section 166 has no application to organizations taxable as corporations.

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[8] *Welch* v. *Bradley*, 130 F. 2d 109 (C. C. A. 1st), the only authority which taxpayer cites does not support its position since a traditional rather than a businesspurpose trust is involved.

CONCLUSION

The decision of the Board of Tax Appeals should be affirmed.

Respectfully submitted,

SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

SEWALL KEY,
HELEN R. CARLOSS,
IRVING I. AXELRAD,
Special Assistants to the Attorney General.

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APPENDIX

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 161. IMPOSITION OF TAX.

(a) *Application of Tax.*—The taxes imposed by this title upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income, which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) *Computation and Payment.*—The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary, except as provided in section 166 (relating to revocable trusts) and section 167 (relating to income for benefit of the grantor). For return made by beneficiary, see section 142.

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

*　　*　　*　　*　　*

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

(c) In the case of income received by estates of deceased persons during the period of administration or settlement of the estate, and in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year, which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary.

*　　*　　*　　*　　*

SEC. 166. REVOCABLE TRUSTS.

Where at any time the power to revest in the grantor title to any part of the corpus of the trust is vested—

(1) in the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom, or

(2) in any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom,

then the income of such part of the trust shall

be included in computing the net income of the grantor.

* * * * *

SEC. 1001. DEFINITIONS.

(a) When used in this Act—

* * * * *

(2) The term "corporation" includes associations, joint-stock companies, and insurance companies.

* * * * *

ART. 1001–1. *Classification of taxables.*—For the purpose of taxation the Act makes its own classification and prescribes its own standards of classification. Local law is of no importance in this connection. Thus a trust may be classed as a trust or as an association (and, therefore, as a corporation), depending upon its nature or its activities. (See article 1001–3.) The term "partnership" is not limited to the common law meaning of partnership, but is broader in its scope and includes groups not commonly called partnerships. (See article 1001–4.) The term "corporation" is not limited to the artificial entity usually known as a corporation, but includes also an association, a trust classed as an association because of its nature or its activities, a joint-stock company, an insurance company, and certain kinds of partnerships. (See articles 1001–2 and 1001–4.) The definitions, terms, and classifications, as set forth in section 1001, shall have the same respective meaning and scope in these regulations.

ART. 1001–2. *Association.*—The term "association" is not used in the Act in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by

a single individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an "investment" trust (whether of the fixed or the management type), an interinsurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Act, a trust or an estate, or a partnership. If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

Art. 1001–3. *Association distinguished from trust.*—The term "trust," as used in the Act, refers to an ordinary trust, namely, one created by will or by declaration of the trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.

As distinguished from the ordinary trust described in the preceding paragraph is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a

declaration or agreement of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a sumstitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages. The nature an dpurpose of a cooperative undertaking will differentiate it from an ordinary trust. The purpose will not be considered narrower than that which is formally set forth in the instrument under which the activities of the trust are conducted.

If a trust is an undertaking or arrangement conducted for income or profit, the capital or property of the trust being supplied by the beneficiaries, and if the trustees or other designated persons are, in effect, the managers of the undertaking or arrangement, whether the beneficiaries do or do not appoint or control them, the beneficiaries are to be treated as voluntarily joining or cooperating with each other in the trust, just as do members of an association, and the undertaking or arrangement is deemed to be an association classified by the Act as a corporation. However, the fact that the capital or property of the trust is not supplied by the beneficiaries is not sufficient reason in itself for classifying the arrangement as an ordinary trust rather than as an association.

By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the advantages of unity of management and continuity of existence which are characteristic of both associations and cor-

porations. This trust form also affords the advantages of capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advantages characteristic of a corporation. These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode or procedure, or effectiveness in action, of an association or a corporation, or as "quasi-corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are attained, in the case of a trust, by the use of the trust form itself. The Act disregards the technical distinction between a trust agreement (or declaration) and ordinary articles of association or a corporate charter, and all other differences of detail. It treats such a trust according to its essential nature, namely, as an association. This is true whether the beneficiaries form the trust or, by purchase or otherwise, acquire an interest in an existing trust.

The mere size or amount of capital invested in the trust is of no importance. Sometimes the activity of the trust is a small venture or enter-

prise, such as the division and sale of a parcel of land, the erection of a building, or the care and rental of an office building or apartment house; sometimes the activity is a trade or business on a much larger scale. The distinction is that between the activity or purpose for which an ordinary strict trust of the traditional type would be created, and the activity or purpose for which a corporation for profit might have been formed.

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